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United States  
Department of  
Agriculture

Forest Service  
Southeastern Area

# Forestry As An Investment In The South



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General Report SA-GR 20

A recent study by the USDA Forest Service shows our nation faces a rising demand for softwood, a demand which soon promises to outstrip supplies at today's prices. The problem is that pine timber stands in the south are being harvested faster than they are being regenerated. To encourage land owners to establish pine stands, the U.S. Government offers a forestry incentives program and tax incentives.

## **FORESTRY INCENTIVES PROGRAM**

The Forestry Incentives Program (FIP) was authorized by Congress in 1973 to share the cost of tree planting and timber stand improvements with private landowners. The Federal share of these costs ranges up to 75 percent, depending upon the cost-share rate set in your particular State and county by the local Agricultural Stabilization and Conservation committee. This cost-share income is generally considered to be tax-free income.

FIP is available in counties designated on the basis of a Forest Service survey of total, eligible, private timber acreage and acreage potentially suitable for production of timber products. To find out if your county participates in this program, check with your county Agricultural Stabilization and Conservation Service office, State forestry agency, or Extension Service office.

## **TAX INCENTIVES**

The U.S. Government also offers the following tax incentives for those who invest in timber:

### **Capital Gains**

Timber qualifies for capital gains tax benefit when sold if the owner has held the timber for 1 year and meets certain qualifications. This means that 60 percent of income from timber sales is excluded from Federal taxes.

### **Public Law 96-451**

New reforestation tax incentives became available with the passage of a new law (PL 96-451) in October 1980. The reforestation incentive is a 10 percent, investment tax credit, plus a 7-year

amortization on the first \$10,000 of capitalized reforestation expenditures each year. The incentive applies to qualifying reforestation expenditures incurred after December 31, 1979. Therefore, capital expenditures for reforestation after 1979 that qualify under this law can be recovered over a period of 7 years — instead of when the timber is harvested. In the South, trees take 20 years or longer to reach harvestable size — a long time to wait to recover your costs, under the rule followed before PL-96-451 was passed.

## Other Tax Considerations

The amount you receive from the timber sale may not be your net income. It's not all clear profit if you have certain types of costs or expenses. You can deduct "expenses of sale" such as:

- tree marking expense
- scaling costs
- cruising costs
- consulting fees
- temporary road construction and improvements connected with the sale with a useful life of 1 year or less.

You can deduct "operating expenses" incurred each year such as:

- Cost of tools of short life (1 year) or small cost
- Equipment maintenance costs
- Salaries, wages and professional fees (excluding your own time)
- Interest on mortgage payments connected with the timber
- Certain taxes connected with the timber
- Depreciation allowance for equipment.

## RECORD KEEPING

Capital gains and tax deductions point up the value of good record keeping by the timber owner. Bookkeeping needn't be complicated. All you need is an orderly list of original costs and expenditures as they are made, backed up by appropriate receipts. Examples:

1. Cost of timber to you: purchase price of property less cost of land and improvements. Record the timber volume at the time of purchase.

2. Establishment costs: site preparation and tree planting.
3. Cost of management services, such as consulting fees.
4. Cultural practices that improve the quality of your timber stand.
5. Timber sales receipts.
6. Up-to-date volume of timber (periodically adjust for growth).

## **HIGH RETURNS POSSIBLE ON FORESTRY INVESTMENTS**

The rate of return on investment is usually quite high from a pine plantation. A return of over 10 percent is common and, in many cases, the rate of return is much higher for a managed plantation. Keep in mind that there are practically no labor cost or capital equipment requirements once the plantation has been established. Also, the rates of return mentioned above are before taxes. When comparing these rates of return with other investments, it's important to realize that the tax advantage available to the timber investor increases the net return dramatically. The rate of return from many other investments before taxes would have to be considerably higher than those mentioned to equal the returns from a pine plantation after taxes.

The chart in the box shows what rate of return an investor can expect when establishing a pine plantation on an average site. It is assumed that the stand will be harvested after 20 years and that stumpage prices will increase 8 percent annually. A 50-cent per acre per year management cost is also assumed.

### **Estimated rate of return on a forestry investment**

Selling price for pulpwood/cord	Establishment cost (\$ per acre)					
	25	50	75	100	125	150
----- percent -----						
8	19.9	16.1	13.9	12.3	11.1	10.1
12	22.4	18.6	16.3	14.7	13.5	12.5
16	24.3	20.3	18.0	16.4	15.1	14.1
20	25.7	21.7	19.4	17.7	16.5	15.4

In most cases the rate of return is even higher than shown in the table if the plantation is carried over a 30-year period, which would allow for the harvesting of both pulpwood and sawtimber.

If you feel you qualify for any of the benefits discussed here, you should seek additional information. Some sources are:

- Your State forestry agency
- Consulting forester
- Qualified tax consultant
- Extension forestry departments of your land-grant university
- Local or district offices of the Internal Revenue Service
- Trust department of some larger banks. Some banks also have foresters on their staff for consulting and management advice.

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